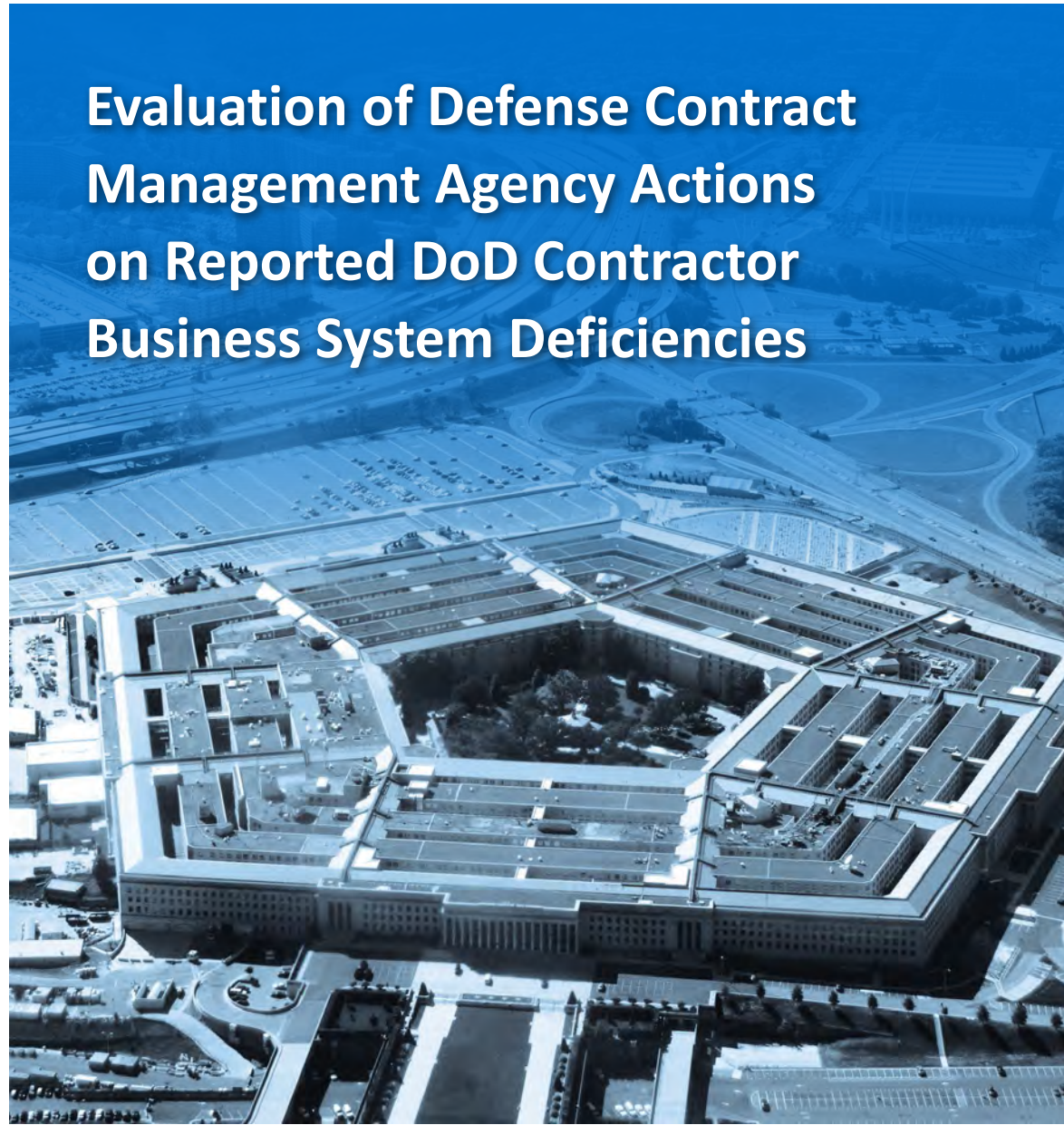




# INSPECTOR GENERAL

*U.S. Department of Defense*

OCTOBER 1, 2015



## Evaluation of Defense Contract Management Agency Actions on Reported DoD Contractor Business System Deficiencies

INTEGRITY ★ EFFICIENCY ★ ACCOUNTABILITY ★ EXCELLENCE

INTEGRITY ★ EFFICIENCY ★ ACCOUNTABILITY ★ EXCELLENCE

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**INSPECTOR GENERAL**  
DEPARTMENT OF DEFENSE  
4800 MARK CENTER DRIVE  
ALEXANDRIA, VIRGINIA 22350-1500

October 20, 2015

MEMORANDUM FOR DIRECTOR, DEFENSE CONTRACT MANAGEMENT AGENCY  
DIRECTOR, DEFENSE CONTRACT AUDIT AGENCY

SUBJECT: Report No. DODIG-2016-0001, "Evaluation of Defense Contract Management Agency Actions on Reported DoD Contractor Business System Deficiencies,"  
October 1, 2015

We are correcting a typographical error on Page iii of the subject report (hereafter referred to as the "transmittal memorandum") that we identified after publishing. Rather than state that the comments we received from Defense Contract Management Agency were partially responsive, we stated that the comments we received from Defense Contract Audit Agency were partially responsive.

Therefore, we are revising the second paragraph of the transmittal memorandum to read "Comments from the Director, Defense Contract Management Agency, were partially responsive." The revised transmittal memorandum is attached. We have revised only the transmittal memorandum, and no other information in the report needed to be modified. Please replace the transmittal memorandum for any copies of the subject report in your possession. You can also access the complete corrected version of the report on our website at <http://www.dodig.mil>.

Please direct questions to me at (703) 604-8877 or at [carolyn.hantz@dodig.mil](mailto:carolyn.hantz@dodig.mil).

A handwritten signature in cursive script, reading "Carolyn R. Hantz", is positioned above the printed name.

Carolyn R. Hantz  
Assistant Inspector General  
Audit Policy and Oversight

Attachment:  
As stated



# Results in Brief

## *Evaluation of Defense Contract Management Agency Actions on Reported DoD Contractor Business System Deficiencies*

**October 1, 2015**

### Objective

We evaluated Defense Contract Management Agency's (DCMA) actions on DoD contractor business system deficiencies reported in 21 Defense Contract Audit Agency (DCAA) audit reports. Our objective was to assess DCMA compliance with the Defense Federal Acquisition Regulation Supplement (DFARS). This is the second of two reports we issued on DCMA compliance with the DFARS requirements.

### Finding

For the 21 DCAA reports we evaluated, DCMA contracting officer actions did not comply with one or more DFARS requirements involving reported business system deficiencies. DCMA contracting officers did not:

- issue timely initial and final determinations,
- obtain or adequately evaluate contractor responses, and
- withhold a percentage of contractor payments.

For example, in 17 of 21 cases, contracting officers did not issue final determination letters within 30 days as DFARS Procedures, Guidance, and Information (PGI) 242.7502(d)(2)(ii)(C) provides. On average, contracting officers took 252 days to issue the final determinations. This likely caused delays in correcting significant business system deficiencies and lengthened the time the Government was unable to rely on data generated by the business systems.

### Finding (cont'd)

In 8 of 21 cases, contracting officers did not withhold a percentage of contractor payments pursuant to DFARS clause 252.242-7005(e). Without a payment withhold, the Government is not protected from the effects of business system deficiencies.

### Management Actions

In response to Report No. DODIG-2015-139, "Evaluation of Defense Contract Management Agency Contracting Officer Actions on Reported Deficiencies Involving DoD Contractors' Estimating Systems," June 29, 2015, DCMA held several training sessions on the business system requirements. In addition, DCMA made business system compliance a special focus during internal reviews, and implemented a tracking tool.

### Recommendations

We recommend that the Director, DCMA:

- review the 21 cases and ensure that contracting officers take appropriate action on the reported business system deficiencies,
- better enforce the use of the business system tracking tool and consider requiring a Board of Review when a contracting officer determines that a reported deficiency is not significant, and
- consider appropriate remedial actions for contracting officers not complying with the DFARS.

### Management Comments and Our Response

In an September 25, 2015, response, the Director, DCMA agreed to the reported recommendations. However, we are requesting additional comments for Recommendation 1.a.

## ***Recommendations Table***

Management	Recommendations Requiring Comment	No Additional Comments Required
Director, Defense Contract Management Agency	1.a	1.b, 2, and 3

Please provide Management Comments by October 30, 2015.



**INSPECTOR GENERAL  
DEPARTMENT OF DEFENSE  
4800 MARK CENTER DRIVE  
ALEXANDRIA, VIRGINIA 22350-1500**

October 1, 2015

MEMORANDUM FOR DIRECTOR, DEFENSE CONTRACT MANAGEMENT AGENCY  
DIRECTOR, DEFENSE CONTRACT AUDIT AGENCY

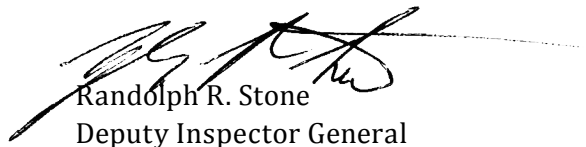
SUBJECT: Report on Evaluation of Defense Contract Management Agency Actions on Reported DoD Contractor Business System Deficiencies (Report No. DODIG-2016-001)

We are providing this report for your review and comment. We evaluated Defense Contract Management Agency's actions on business system deficiencies reported in 21 Defense Contract Audit Agency reports. In several instances, contracting officers did not comply with the requirements of Defense Federal Acquisition Regulation Supplement clauses 252.242-7006 and 252.242-7005 for issuing timely initial and final determinations, obtaining and evaluating the contractor's response to the reported deficiencies, and withholding payments for uncorrected deficiencies.

We considered management comments on a draft of this report. DoD Instruction 7650.03 requires that recommendations be resolved promptly. Comments from the Director, Defense Contract Management Agency, were partially responsive. We request additional comments on Recommendation 1.a by October 30, 2015.

Please provide comments that conform to the requirements of DoD Instruction 7650.03. Please send a PDF file containing your comments to the e-mail address included in the last paragraph of this memorandum. Copies of your comments must have the actual signature of the authorizing official for your organization. We cannot accept the /Signed/ symbol in place of the actual signature. If you arrange to send classified comments electronically, you must send them over the SECRET Internet Protocol Router Network (SIPRNET).

We appreciate the courtesies extended to the staff. Please direct questions to Ms. Carolyn R. Hantz at (703) 604-8877, or e-mail at [carolyn.hantz@dodig.mil](mailto:carolyn.hantz@dodig.mil).

  
Randolph R. Stone  
Deputy Inspector General  
Policy and Oversight

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## Acronyms and Abbreviations

# Introduction

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## Objective

We evaluated Defense Contract Management Agency (DCMA) actions on DoD contractor business system deficiencies reported by the Defense Contract Audit Agency (DCAA). Our primary objective was to determine if DCMA complied with applicable Defense Federal Acquisition Regulation Supplement (DFARS) requirements. For example, we evaluated DCMA contracting officer actions on accounting system deficiencies for compliance with:

- DFARS clauses 252.242-7005, “Contractor Business Systems,” and 252.242-7006, “Accounting System Administration” and
- DFARS Procedures, Guidance, and Information (PGI) 242-7502, “Contractor Accounting Systems and Related Controls.”

As part of the evaluation, we randomly selected 21 of 164 DCAA business system deficiency reports issued from July 2012 through June 2013. See Appendix A for a discussion of our scope and methodology. This is the second of two reports we issued on DCMA contracting officer compliance with the DFARS requirements relative to contractor business systems. Our first report addressed an evaluation of DCMA contracting officer actions on reported DoD contractor estimating system deficiencies. This report addresses our evaluation of contracting officer actions on other contractor business systems, including accounting, billing, and material management and accounting systems.

## Background

### ***Business System Requirements***

Contractor business systems and related internal controls are the first line of defense against waste, fraud, and abuse. A DoD contractor’s accounting and billing systems encompass the policies, procedures, practices, and controls used by the contractor to gather, record, classify, analyze, summarize, interpret, and present accurate and timely financial data for reporting in compliance with applicable laws, regulations, and management decisions.

Inadequacies with contractor business systems led to the enactment of major changes to related DoD regulations. On February 24, 2012, DoD revised the DFARS addressing contractor business systems to incorporate time limits for taking action on reported business system deficiencies and to require payment withholding if the system is disapproved. For example, DFARS PGI 242.75, “Contractor Accounting



Systems and Related Controls,” states that the contracting officer should issue a final determination on reported deficiencies within 30 days after receiving the contractor’s response to the initial determination of deficiencies.

For contracts that include DFARS clause 252.242-7005(e), “Withholding Payments,” contracting officers must withhold 5 percent of payments from a DoD contractor if significant deficiencies exist with any of the contractor’s business systems.

### ***Defense Contract Audit Agency***

DCAA performs contract audits for DoD and performs contract audit services for non-DoD Federal organizations on a reimbursable basis. DCAA operates in accordance with DoD Directive 5105.36, “Defense Contract Audit Agency,” January 4, 2010, and reports to the Under Secretary of Defense (Comptroller)/Chief Financial Officer.

The Agency performs several types of contract audits, such as audits of contractor claimed incurred costs, forward-pricing proposals, and contractor business systems. In FY 2014, DCAA examined \$183 billion in contract costs that were processed through DoD contractor business systems. If DCAA uncovers a significant business system deficiency during a system review or other related audit, DCAA policy requires that the auditor issue a “deficiency report” to alert the cognizant DCMA contracting officer of the deficiency and recommend contractor corrective action. Between July 2012 and June 2013, DCAA issued 164 business system deficiency reports.

### ***Defense Contract Management Agency***

DCMA is a component of the DoD that works directly with DoD contractors to ensure that DoD, Federal, and allied government supplies and services are delivered on time and at projected cost, and meet all performance requirements.

DCMA contracting officers are responsible for several contract administrative functions, such as approving or disapproving contractor business systems, determining final indirect cost rates on cost-reimbursement contracts, and evaluating contractor compliance with the Cost Accounting Standards. DCMA contracting officers are required to consider any DCAA business system deficiency reports and other expert advice to help them determine whether to approve or disapprove contractor business systems.

For the 21 DCAA reports we selected for evaluation, DCMA contracting officers were responsible for determining the adequacy of the contractor’s business systems and taking action required by DFARS clause 252.242.7006 and DFARS PGI 242.7502.

## Finding

### Contracting Officers Did Not Comply With DFARS Requirements and DCMA Policy

For all 21 DCAA reports we evaluated, DCMA contracting officers did not comply with one or more DFARS requirements. Each DCAA report outlined significant business system deficiencies that impacted DoD's ability to rely on information produced by the system. DCMA contracting officers did not take appropriate or timely action to address the significant business system deficiencies DCAA had reported.

### Scope of Evaluation

We evaluated DCMA contracting officer actions on 21 DCAA reports of contractor business system deficiencies to determine whether the actions complied with DFARS requirements and DCMA instructions. DFARS clause 252.242-7005(b), "Contractor Business Systems," defines a significant deficiency as a shortcoming in the system that materially affects the ability of DoD officials to rely upon information produced by the system that is needed for management purposes. Examples of deficiencies reported by DCAA included the contractor's failure to:

- ensure that direct material and labor costs were charged to the appropriate contract,
- notify the Government of cost accounting changes within 60 days,
- perform adequate or periodic reviews of its accounting system and rate structure, and
- comply with labor categories specified in the contract.

These types of deficiencies can materially impact the Government's ability to rely on information produced by a contractor's business system.

For each DCAA report, our evaluation primarily focused on whether the contracting officer:

1. issued an initial determination on reported significant deficiencies within 10 days in accordance with DFARS PGI 242-7502(d)(2)(ii)(A);
2. obtained a written contractor response to the initial determination within 30 days pursuant to DFARS clause 252.242-7006(d)(2);
3. evaluated the contractor's response as discussed in DFARS PGI 242-7502(d)(2)(ii)(C);
4. issued a final determination to approve or disapprove the system within 30 days in accordance with DFARS PGI 242-7502(d)(2)(ii)(C); and

5. withheld a percentage of payments from contractor billings to the Government in accordance with DFARS Clause 252.242-7006(e), if the system is disapproved.

## Results of Evaluation

For the 21 DCAA deficiency reports we selected for evaluation, Table 1 depicts the instances when DCMA contracting officers did not comply with the five DFARS key requirements we evaluated.

*Table 1. Results of Evaluation on Actions Taken in Response to 21 DCAA Accounting System Deficiency Reports*

DCAA Report No.	Contracting Officer Actions That Did Not Comply With DFARS				
	Initial Determination	Obtain Contractor Response	Evaluation of Contractors Response	Final Determination	Withhold of Contractor Payments
01211-2013D11090002	X	X		X	
01311-2013J11090001			X		
01701-2012E11070002		X	X		
01701-2012E11090001		X	X		
06151-2012F11070003	X			X	
06811-2011U11070002	X	X	X	X	
06811-2012U11070004	X		X	X	
01211-2012D11090001		X	X	X	
03911-2011P12500001	X	X		X	
03911-2012P11090001	X	X		X	
04231-2012V11070001	X		X		X
04421-2012G11070001	X	X	X	X	X
04551-2012B11090002	X	X	X	X	X
09821-2011C12500002 S-1	X		X	X	
06151-2011E11010001	X	X	X	X	X
01291-2013F11010101	X		X	X	X
03311-2012W11090001	X	X	X	X	X
03911-2013I11090001	X			X	
06211-2013C11090001	X	X	X	X	X
09881-2012C11070003	X		X	X	
03321-2013N11090002	X	X	X	X	X
<b>Total Instances of Non-Compliance</b>	<b>17</b>	<b>13</b>	<b>16</b>	<b>17</b>	<b>8</b>
<b>Non-Compliance Rate</b>	<b>81%</b>	<b>62%</b>	<b>76%</b>	<b>81%</b>	<b>38%</b>

## ***Contracting Officers Did Not Timely Issue Initial Determinations***

### ***DFARS Criteria and DCMA Instructions on Initial Determinations***

DFARS PGI 242.7502(d)(2)(ii)(A) states,

Within 10 days of receiving the DCAA report, if the contracting officer makes a determination that there is a significant deficiency, the contracting officer should provide an initial determination of deficiencies and a copy of the report to the contractor and require the contractor to submit a written response.

The initial determination involves the contracting officer making a preliminary assessment as to whether a significant deficiency may exist based on their review of DCAA reported findings. In the initial determination letter, the contracting officer describes each significant deficiency in sufficient detail to allow the contractor to understand the deficiency.

DCMA Instruction 131, "Contractor Business Systems," paragraph 3.2.2, requires supervisor approval of all proposed initial determinations before issuance.

### ***Contracting Officer Actions Did Not Comply With DFARS Regarding Initial Determinations***

For 17 of 21 cases we evaluated, DCMA contracting officers did not comply with the DFARS PGI requirements for issuing an initial determination. In four instances, the contracting officers never issued the required initial determination letter. In one instance, the contracting officer did not require the contractor to provide a written response to the initial determination. In the remaining 12 instances, the contracting officers issued determination letters, but they were not issued within the 10-day standard. On average, contracting officers took 91 days to issue the 12 initial determination letters. The contracting officers' failure to issue timely initial determination letters likely resulted in delays and lengthened the time the Government was unable to rely on the financial data produced by the contractor's system.

For 1 of the 12 instances, the contracting officer also did not require the contractor to provide a written response to the initial determination.

Finally, in eight instances, we found no evidence of a supervisor approving the initial determination letter, as DCMA Instruction 131, paragraph 3.2.2 requires. The lack of supervisory approval diminishes DCMA management oversight of contracting officer actions on business systems.

## ***Contracting Officers Did Not Follow Up With Contractors on Overdue and Incomplete Responses***

### ***DFARS Criteria for Obtaining a Contractor's Response***

DFARS clause 252.242-7006(d)(2) requires the contractor to respond in writing within 30 days of receiving the contracting officer's initial determination that identified significant system deficiencies.

Obtaining a contractor's written response expedites the corrective action process for resolving the reported deficiencies. A timely contractor response is necessary to ensure that the contracting officer promptly receives either notice that the deficiencies have been corrected or an acceptable corrective action plan showing milestones and actions to eliminate the reported deficiencies.

### ***Contracting Officer Did Not Follow Up on Overdue and Incomplete Contractor Responses***

In 13 of the 21 cases we evaluated, the contracting officer did not take appropriate action when a contractor's response became overdue (exceeded 30 days), or was incomplete. In four of these instances, the contractor did not provide a response to the contracting officer. In nine instances, the contracting officer received a response, but after the 30-day timeframe outlined in DFARS. On average, the contracting officer received the nine responses 170 days after issuing the initial determination. Once the contractor responses became overdue, the DCMA contract file lacked evidence that the contracting officers had followed up with the contractor to obtain the responses.

An untimely contractor response to the initial determination may cause system deficiencies to remain uncorrected, thereby diminishing the reliability that can be placed on the accuracy of the financial data reported by the contractor's system.

## ***Contracting Officers Did Not Adequately or Timely Evaluate the Contractor's Responses to the Initial Determination***

### ***DFARS Criteria for Evaluating the Contractor's Response***

DFARS PGI 242.7502(d)(2)(C) states,

Within 30 days of receiving the contractor's response, the contracting officer, in consultation with the auditor or cognizant functional specialist, should evaluate the contractor's response and make a final determination.

The contracting officer is responsible for evaluating the sufficiency of the contractor's response on the initial determination to determine whether the contractor addressed all significant deficiencies. If the contractor includes a



corrective action plan in its response, the contracting officer is required to verify the proposed actions and the milestones to eliminate the deficiencies in consultation with the auditor.

### *DCMA Did Not Perform an Adequate or Timely Evaluation of Contractor Responses*

For 16 of the 21 cases, contracting officers did not comply with the DFARS requirement for evaluating the contractor's response, including:

- 3 cases lacking evidence that the contracting officers had evaluated the contractor's response to the reported deficiencies;
- 5 cases when contracting officers failed to perform an adequate evaluation of the contractor's response;
- 3 cases when contracting officers did not perform an adequate evaluation and did not complete the evaluation within 30 days; and
- 5 cases when contracting officers completed the evaluation beyond the 30-day timeframe.

Regarding the untimely evaluations, contracting officers took 261 days on average to complete their evaluation of the contractor's response. To protect the Government's interests, the contracting officer has an obligation to evaluate the contractor's response in order to verify that the contractor's proposed actions fully address the reported deficiencies. Without conducting an adequate evaluation, the contracting officer may not detect that the proposed corrective actions are insufficient to eliminate significant deficiencies.

### ***Contracting Officers Did Not Issue Final Determinations in a Timely Manner***

#### *DFARS Criteria for Final Determinations*

DFARS PGI 242.7502(d)(2)(ii)(C) states the contracting officer should issue a final determination within 30 days of receiving the contractor's response. The final determination reflects the contracting officer's ultimate decision on whether to approve or disapprove the business system.

DFARS clause 252.215-7002(e)(3) states,

The Contracting Officer will evaluate the Contractor's response and notify the Contractor, in writing, of the Contracting Officer's final determination concerning (i) Remaining significant deficiencies; (ii) The adequacy of any proposed or completed corrective action; and (iii) System disapproval, if the Contracting Officer determines that one or more significant deficiencies remain.

DCMA Instruction 131, paragraph 2.3, states that a DCMA contracts director is responsible for reviewing and approving all final determinations of a contractor business system before issuance. DCMA Instruction 131, paragraph 3.4.1, also requires approval from a DCMA contracts director if the contracting officer anticipates taking more than 30 days to issue a final determination.

### *Contracting Officer Actions Did Not Comply With DFARS Criteria for Final Determinations*

In 17 of the 21 cases, the contracting officer did not comply with the DFARS requirement for making a final determination on a contractor business system. In three cases, the contracting officer did not issue a final determination. In the remaining 14 cases, the contracting officer took more than 30 days to issue the final determination. DCMA took 252 days on average to issue the 14 determinations. The contracting officers also did not obtain the required approval for exceeding the 30-day DFARS standard as DCMA Instruction 131, paragraph 3.4.1, requires.

Furthermore, in 2 of the 14 cases, the contracting officer did not obtain the required approval for issuing the final determination as DCMA Instruction 131, paragraph 2.3, requires.

The failure to make a timely final determination increases the Government's risk that significant business system deficiencies remain uncorrected, thereby diminishing the Government's ability to rely on the data produced by the system. Making a final determination in a timely manner is important when the system is disapproved, because it triggers the requirement to withhold payments and to protect the Government's interests.

### ***Contracting Officers Did Not Disapprove the Contractor's System and Withhold Payments***

#### *DFARS Criteria for Implementing Payment Withholds*

DFARS clause 252.242-7005(e) states that if the contracting officer disapproves the accounting system, the contracting officer will withhold 5 percent of contractor billings until the contracting officer has determined that the contractor corrected all significant deficiencies.

DFARS clause 252.242-7006(f) requires that if the contracting officer makes a final determination to disapprove the contractor's accounting system, the contracting officer will withhold payments on contracts that include DFARS clause 252.242-7005.

### *Contracting Officer Actions Did Not Comply With DFARS Requirements for Withholding Payments*

In 8 of 21 cases, DCMA contracting officers did not withhold payments even though significant deficiencies remained or could have remained. In two of eight instances, the contracting officer elected not to disapprove the contractor's system and implement payment withholds even though he determined that significant deficiencies existed. For the remaining six instances, the contracting officer approved the system without performing an adequate evaluation of the contractor's corrective actions. Without an adequate evaluation of the contractor's corrective actions, the contracting officers could have approved the business systems without detecting that significant deficiencies still existed. If significant system deficiencies still existed, the contracting officer had an obligation to disapprove the system and implement payment withholdings to protect the Government's interests.

## **DCMA Internal Controls Related to Business Systems**

### ***DCMA Business System Tracking Tool***

Since August 2013, DCMA has maintained a spreadsheet referred to as the "Contractor Business System Determination Timeline Tracking Tool." The Tool tracks key milestone dates from receipt of a DCAA audit report to issuance of a final determination. DCMA management uses the tool to monitor the status of contracting officer actions on reported business system deficiencies and to take corrective actions when appropriate. DCMA designed the Tool to ensure that contracting officers issue determinations and evaluate contractor responses in a timely manner.

For 10 of 21 cases we evaluated, contracting officers were required to track the key milestone dates in the Tool. In five cases, the contracting officer failed to use the tool and track the key milestone dates as required. DCMA should better enforce its use of the Tool, which is an important control for ensuring that contracting officers issue determinations and evaluate contractor responses in a timely manner.

### ***DCMA Board of Review Process***

DCMA Instruction 134, "Board of Review," states that certain contracting actions are subject to an additional level of review referred to as the Headquarters Board of Review. According to DCMA Instruction 131, a DCMA Headquarters "Board of Review" is required when the contracting officer rejects the auditor's advice on a reported business system deficiency. The Instruction states that a rejection of advice occurs when a contracting officer and DCAA disagree on whether a deficiency in a business system exists. However, the Instruction also states that a Board of Review is not required when the contracting officer agrees that a

deficiency exists, but rejects DCAA's opinion that the deficiency is significant. The DFARS requirements for business systems, such as the need to issue timely determinations and to withhold payments, apply only to "significant" business system deficiencies.

In 4 of 21 cases, contracting officers were required to obtain a Board of Review before issuing their final determination. However, in one of the four cases (25 percent), the contracting officer failed to obtain the required review. DCMA should take action to better enforce the requirement for obtaining a Board of Review.

For five additional cases, contracting officers had rejected DCAA's opinion that the reported deficiencies were significant. However, the DCMA contract files for three of the five cases (60 percent) lacked adequate rationale for rejecting the auditor's opinion and concluding that the deficiencies were not significant. For example, for two of the three cases, DCAA reported inadequacies related to the contractor's failure to properly identify expressly unallowable costs and to support costs claimed on Government contracts. These inadequacies appear to qualify as significant deficiencies outlined in DFARS clause 252.242-7006(a)(3). Although the contracting officer concluded that these deficiencies warranted corrective actions, she determined they were not significant and she did not document adequate rationale for her determination.

When used, the Board of Review is an effective tool for evaluating the appropriateness of contracting officer actions on reported business systems deficiencies. DCMA should consider requiring a Board of Review in all cases when contracting officers reject DCAA advice, including rejections involving the significance of a reported deficiency. This change should help to provide reasonable assurance that contracting officers take appropriate actions on business system deficiencies prior to approving the system.

## **Previous DoD IG Finding and DCMA Management Actions**

On June 29, 2015, we issued Report No. DODIG-2015-139, "Evaluation of Defense Contract Management Agency Contracting Officer Actions on Reported Deficiencies Involving DoD Contractors' Estimating Systems." Regarding 17 of 18 DCAA-reported estimating deficiencies we evaluated, contracting officers did not issue initial or final determinations, in a timely manner, did not promptly and adequately evaluate the contractor's response to significant estimating system deficiencies, and failed to disapprove the system and implement payment withholds. We recommended that the DCMA Director improve related controls, conduct training, and implement withholds from the contractors' payments when appropriate.

In response, DCMA developed a corrective action plan on the 18 estimating system cases we evaluated and held several training sessions in 2015 to refresh its workforce on DFARS business system requirements. In addition, DCMA's "Mission Review Team" made business system compliance a special focus item during its internal reviews. Finally, DCMA pointed out that it had implemented the Contractor Business Determination Timeline Tracking Tool in August 2013.

## Conclusion

In response to Report No. DODIG-2015-139, DCMA is taking positive steps to improve its actions on reported estimating deficiencies. Nevertheless, for the 21 reports we selected for this evaluation, we found continued inadequacies with the actions contracting officers took on significant accounting, billing, and material management and accounting system deficiencies. The inadequacies are similar to those reported in Report No. DODIG-2015-139. For example, we found that contracting officers did not issue initial or final determinations, in a timely manner, adequately evaluate the contractor's response to significant deficiencies, and implement payment withholdings for existing significant deficiencies.

In addition to the positive steps DCMA is taking, DCMA should better enforce its requirements for using the Contractor Business System Determination Timeline Tracking Tool and requesting a Board of Review. In addition, DCMA should consider requiring a Board of Review for all rejections of DCAA advice, including those involving the significance of reported deficiencies. These additional steps should help to ensure that contracting officers comply with the DFARS business system requirements and protect the Government's interests when contractor business systems contain significant deficiencies.

## Recommendations, Management Comments, and Our Response

### ***Recommendation 1***

**We recommend that the Director, Defense Contract Management Agency review the 21 cases we evaluated and ensure that contracting officers:**

- a. Take all appropriate actions in response to reported business system deficiencies, including the issuance of initial and final determinations and disapproval of any systems that have significant uncorrected deficiencies.**

### ***Director, Defense Contract Management Agency Comments***

The Director, Defense Contract Management Agency agreed. DCMA will develop a corrective action plan for those cases with outstanding actions. Due to the complex nature of some cases, the Director stated that contracting officers may



need additional time beyond the timeline goals set forth in the DFARS in order to complete the required actions. Also, the Director provided specific comments on 4 of the 21 cases to explain why she believes the contracting officers complied with the DFARS and that no corrective actions are required.

### *Our Response*

The Director, DCMA comments are partially responsive. We considered the Director's specific comments on the four cases. We still find that the contracting officers did not comply with the DFARS requirements and DCMA should take appropriate action to comply with the DFARS. Appendix C provides details concerning management comments and our response on each of the four cases. We request that the Director reconsider her responses on the four cases and provide additional comments.

- b. Implement payment withholds on any disapproved business systems when the clause at Defense Federal Acquisition Regulation Supplement 252.242-7005(e) is included in the contract.**

### *Director, Defense Contract Management Agency Comments*

The Director, DCMA agreed and indicated that DCMA will disapprove those systems with any remaining significant deficiencies and identify contracts eligible for payment withhold in accordance with agency procedures.

### *Our Response*

The Director, DCMA comments to the recommendation are responsive and no additional comments are required.

## **Recommendation 2**

**We recommend that the Director, Defense Contract Management Agency:**

- a. Better enforce the requirements for using the Contractor Business System Determination Timeline Tracking Tool and requesting a Board of Review.**

### *Director, Defense Contract Management Agency Comments*

The Director, DCMA agreed, stating that the internal controls should be periodically reviewed to ensure that they are operating effectively and enhanced as needed. The Director noted that the failure to use the tracking tool in some cases was due to a "learning curve" associated with the new tool.

Regarding the Board of Review, the Director stated that DCMA Instruction 134 provides guidance for contracting officers to obtain a Board of Review when they reject the advice of an auditor. However, DCMA believes a Board of Review is not warranted when the contracting officer concludes that a reported deficiency is not significant.

### *Our Response*

The Director, Defense Contract Management Agency comments are responsive and no additional comments are required.

- b. Consider requiring that contracting officers request a Board of Review when they reject an auditor's opinion based on the significance of a business system deficiency.**

### *Director, Defense Contract Management Agency Comments*

The Director considered requiring the contracting officers to request a Board of Review when they reject an auditor's opinion based on the significance of a business system deficiency. The Director concluded that the determination of significance is within the contracting officer's authority and responsibility. Therefore, DCMA will not require the contracting officer to request a Board of Review.

### *Our Response*

The Director, Defense Contract Management Agency comments to the recommendation are generally responsive. We appreciate the Director's consideration of our recommendation and we therefore do not require additional comments.

Nevertheless, we maintain that the implementation of our recommendation has the potential to significantly enhance DCMA's internal controls for ensuring compliance with the DFARS requirements related to contractor business systems.

As previously discussed in the "DCMA Board of Review Process" paragraph, we found several instances when contracting officers had rejected DCAA's opinion that the reported deficiencies were significant. In most cases, the DCAA-reported deficiencies appeared to qualify as significant deficiencies outlined in DFARS clause 252.242-7006(a)(3), and the contracting officer did not document adequate rationale for concluding that the deficiencies were insignificant. An additional assessment by the Board of Review would help to ensure that the contracting officer has appropriately addressed the audit findings and documented adequate rationale in the contract file.

### ***Recommendation 3***

**Consider appropriate remedial actions as a result of contracting officers not complying with the Defense Federal Acquisition Regulation Supplement for issuing initial and final determinations, obtaining and evaluating the contractor's response, and withholding payments.**

#### ***Director, Defense Contract Management Agency Comments***

The Director, Defense Contract Management Agency agreed. The Director will consider appropriate remedial actions when contracting officers willfully do not comply with the Defense Federal Acquisition Regulation Supplement and agency policy for issuing initial and final determinations, obtaining and evaluating the contractor's response, and withholding payments. The Director stated any remedial action will be based upon a consideration of the circumstances and the complexity of the situation.

#### ***Our Response***

The Director, Defense Contract Management Agency comments to the recommendation are responsive and no additional comments are required.

It should be noted, however, that remedial action should not be limited to those instances when a contracting officer "willfully" did not comply with the DFARS requirements and agency policy. For example, DCMA management may also need to consider remedial action if a contracting officer fails to exercise due diligence, lacks appropriate training, or is negligent in applying the DFARS requirements.

## Appendix A

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### Scope and Methodology

We conducted this evaluation from November 2014 through June 2015 in accordance with the Council of Inspectors General on Integrity and Efficiency “Quality Standards for Inspection and Evaluation.” As part of the evaluation, we randomly selected 21 of 164 business system deficiency reports from a listing of reports that DCAA issued between July 2012 and June 2013. To accomplish our objective, we:

- obtained and gained an understanding of the business system deficiencies outlined in the 21 DCAA reports we selected for evaluation;
- interviewed appropriate DCMA and DCAA employees;
- analyzed relevant DCAA and DCMA documents; and
- evaluated DCMA contracting officer actions for compliance with DFARS PGI 242.7502, and DFARS clauses 252.215-7002, 252.242-7005, and 252.242-7006.

### Use of Computer-Processed Data

In selecting the 21 DCAA audit reports, we relied on a computerized listing of DCAA deficiency reports issued between July 2012 and June 2013. DCAA generated the listing from its Management Information System. We did not selectively test the listing for accuracy and completeness.

### Use of Technical Assistance

The DoD Inspector General’s Quantitative Methods Division assisted us in selecting a sufficient cross-section of DCAA reports for evaluation.

### Prior Report Coverage

During the last 5 years, the DoD IG has issued three reports related to DCMA’s actions on business system deficiencies reported by DCAA. The following unrestricted DoD IG reports can be accessed over the Internet at <http://www.dodig.mil>.

DoD IG Report No. DODIG-2015-139, “Evaluation of Defense Contract Management Agency Contracting Officer Actions on Reported Deficiencies Involving DoD Contractors’ Estimating Systems,” June 29, 2015

DoD IG Report No. DODIG-2014-084, "Hotline Allegations Regarding Defense Contract Management Agency Contracting Officer Actions on Several Business System Audit Reports," June 20, 2014

DoD IG Report No. D-2010-6-002, "Allegation of Unsatisfactory Conditions Regarding Actions by the Defense Contract Management Agency Earned Value Management Center," July 28, 2010



## Appendix B

### Selected DCAA Reports and Responsible DCMA Field Office

Table B. Selected DCAA Reports and Responsible DCMA Field Office

Count	DCAA Report No.	DCAA Report Date	Responsible DCMA Field Office
1	01211-2013D11090002	12/14/2012	Nashville
2	01311-2013J11090001	03/08/2013	Space Coast
3	01701-2012E11070002	11/26/2012	North Coast
4	01701-2012E11090001	10/22/2012	Northern Ohio
5	06151-2012F11070003	10/05/2012	Fairfax
6	06811-2011U11070002	07/13/2013	York
7	06811-2012U11070004	08/9/2012	York
8	01211-2012D11090001	01/16/2013	Nashville
9	03911-2011P12500001	08/08/2012	Utah
10	03911-2012P11090001	09/05/2012	Utah
11	04231-2012V11070001	05/13/2013	San Fernando
12	04421-2012G11070001	05/10/2013	South Bay
13	04551-2012B11090002	10/30/2012	La Jolla
14	09821-2011C12500002 S-1	02/13/2013	Valley Forge
15	06151-2011E11010001	08/02/2012	Fairfax
16	01291-2013F11010101	02/13/2013	Charlotte
17	03311-2012W1109001	12/13/2012	Arlington
18	03911-2013I11090001	02/22/2013	Utah
19	06211-2013C11090001	04/15/2013	Falls Church
20	09881-2012C11070003	08/10/2012	Dulles
21	03321-2013N11090002	12/31/2012	Houston

## Appendix C

### Details of DCMA Management Comments and Our Responses to Four Cases

Table C. Details of DCMA Management Comments and Our Responses to Four Cases

Case / DCAA Report Number	Area of Non-compliance	DCMA Comments	DoDIG Response
4231-2012V110700001	<ul style="list-style-type: none"> <li>Withhold of Contractor Payments</li> </ul>	The contracting officer approved the accounting system. Withholds do not apply when the system is approved.	The contracting officer did not adequately evaluate the contractor's corrective actions. For example, the contracting officer did not verify that the corrective actions were implemented or effective to justify approving the system. Withholdings may be needed if the contracting officer performs an adequate evaluation and the deficiencies still remain.
4421-2012G110700001	<ul style="list-style-type: none"> <li>Initial Determination</li> <li>Obtain Contractor Response</li> <li>Evaluation of Contractor Response</li> <li>Final Determination</li> <li>Withhold of Contractor Payments</li> </ul>	There was no requirement to issue a business system determination since the audit was based on a contractor's firm fixed price (FFP) subcontract proposals. The contractor did not have any prime contracts that are cost type contracts or any FFP contracts with progress payments/financing during this timeframe.	DFARS clause 252.242-7005(a), "Contractor Business Systems" states, "this clause only applies to covered contracts that are subject to the Cost Accounting Standards." We request DCMA to provide documentary evidence to show that, during 2012 and 2013, the contractor performed on contracts were exempt from the Cost Accounting Standards (CAS) in accordance with FAR 9903.201-1, "CAS Applicability."
3311-2012W110900001	<ul style="list-style-type: none"> <li>Withhold of Contractor Payments</li> </ul>	The contracting officer issued a final determination on May 1, 2013 approving the system, so withhold does not apply.	The contracting officer did not verify the assertions made in the response to justify approving the system. Withholdings may be needed if the contracting officer verifies the assertions and finds that deficiencies still remain.

*Table C. Details of DCMA Management Comments and Our Responses to Four Cases (cont'd)*

Case / DCAA Report Number	Area of Non-compliance	DCMA Comments	DoDIG Response
3321-2013N11090002	<ul style="list-style-type: none"><li>• Withhold of Contractor Payments</li></ul>	The contracting officer's final determination letter did not consider the cited deficiencies to be significant enough to change the approved system status. Withholds do not apply to approved systems.	Although the contracting officer concluded that the cited deficiency is not significant, he did not provide a rationale for his conclusion. The contracting officer should document an adequate rationale, or reconsider his conclusion and withhold payments if he is unable to adequately document his prior decision.

## Management Comments

### Defense Contract Management Agency



**DEFENSE CONTRACT MANAGEMENT AGENCY**  
3901 A AVENUE, BUILDING 10500  
FORT LEE, VA 23801-1809

SEP 25 2015

MEMORANDUM FOR DEPARTMENT OF DEFENSE, DEPUTY INSPECTOR GENERAL,  
POLICY AND OVERSIGHT

SUBJECT: Report on Evaluation of Defense Contract Management Agency Contracting  
Officer Actions on Reported DoD Contractor Business System Deficiencies  
(Project No. D2013-DAPOCF-0201.002)

This is in response to your August 11, 2015 draft report regarding DCMA contracting  
officer actions on reported deficiencies involving contractor business systems.

OIG Recommendations:

We recommend that the Director, DCMA:

1. Review the 21 cases we evaluated and ensure that contracting officers:

a. Take all appropriate actions in response to reported accounting system  
deficiencies, including the issuance of initial and final determinations and disapproval of any  
systems that have significant uncorrected deficiencies; and

b. Implement payment withholds on any disapproved business system when the  
clause at Defense Federal Acquisition Regulation Supplement (DFARS) 252.242-7005(e) is  
included in the contract.

2. Enhance related internal controls by:

a. Better enforcing the requirements for using the Contractor Business System  
Determination Timeline Tracking Tool and requesting a Board of Review; and

b. Consider requiring that contracting officers request a Board of Review when  
they reject an auditor's opinion based on the significance of a business system deficiency.

3. Consider appropriate remedial actions as a result of contracting officers not complying  
with the Defense Federal Acquisition Regulation Supplement for issuing initial and final  
determinations, obtaining and evaluating the contractor's response, and withholding payments.

**DCMA Response: 1.a. Concur.** I agree that all appropriate actions in response to  
reported accounting system deficiencies should be taken in accordance with the applicable  
DFARS and policy guidance. As such, we have reviewed the 21 system cases and concur with  
your findings except for those identified in green on Table 1. We will develop a Corrective  
Action Plan (CAP) by September 30, 2015 for those cases with outstanding actions. Worth

## Defense Contract Management Agency (cont'd)

noting, however, is that the business system determination timelines are goals set forth in policy and may require additional time due to the complex nature of some cases.

DCAA Report	Report Date	Contracting Officer Actions That Did Not Comply With DFARS Based on DODIG Evaluation					DCMA Review & Comments
		Initial Determination	Obtain Contractor Response	Evaluation of Contractor's Response	Final Determination	Withhold of Contractor Payments	
D-231-2012V11070001	05/13/2013	X		X		X	Even though the contracting officer performed a sole evaluation of the contractor's corrective action a final determination was issued on 5/23/2014 approving the Material Management and Accounting System and on 9/22/2014 approving the Accounting System. Withholds do not apply when a system is approved.
D-421-2012G11070001	05/10/2013	X	X	X	X	X	This audit was not in Contract Audit Follow Up (CAFU) eTool and as it relates to subcontracts only/no prime contracts. Subcontract audits are not included in the CAFU export from DCAA. There was no requirement to issue business system determination since the audit was based on contractor's Firm Fixed Price (FFP) subcontract proposals. The contractor did not have any prime contracts that are cost type contracts or any FFP contracts with progress payments/financing during this timeframe.
D-311-2012W11090001	12/13/2012	X	X	X	X	X	The contracting officer issued a final determination on 5/1/2013 approving the system so withholds do not apply.
D-321-2013N11090002	12/31/2012	X	X	X	X	X	The Final Determination dated 2/5/2014 states the contracting officer did not consider the cited deficiencies to be significant enough to warrant a change to the Approved system status. The contracting officer addressed/justified the deficiency determination in the Memorandum For Record dated 2/5/2014. Withholds do not apply to approved systems.

Table 1. Results of DoDIG Evaluation and DCMA Response

**DCMA Response: 1.b. Concur.** In general, I agree that contracting officers should implement payment withholds on disapproved business systems in accordance with DFARS 252.242-7005, Contractor Business Systems. DFARS 242.7000(b)(1), however, states contracts for withhold are to be identified in accordance with agency procedures. Consequently, not all contracts that contain DFARS 252.242-7005 are candidates for payment withhold. DCMA Instruction 131, Contractor Business Systems, specifies withhold candidates shall include all contracts that: (1) contain DFARS 252.242-7005; (2) contain the applicable business system specific clause (i.e., DFARS 252.242-7006, Accounting System Administration); and (3) have a total contract value greater than or equal to \$50 million. We chose this threshold based on a May 2010 analysis of contracts that found 93% of total contract dollars are on contracts valued at \$50 million or more. Focusing on this population gives the Government the best return and mitigation while still incentivizing contractors to correct their system deficiencies as having a disapproved system may preclude award of future contracts.

Moreover, withholds are not the only remedy contracting officers can use to incentivize contractors to take corrective action on deficient business systems. Other remedies such as a reduction in contract financing, suspension of progress payments, or revocation of the Government's assumption of risk for loss of property are also available when applicable. Therefore, as part of our CAP, we will disapprove those systems with any remaining significant deficiencies and identify contracts for payment withhold in accordance with agency procedures.



## Defense Contract Management Agency (cont'd)

**DCMA Response: 2.a. Concur.** I agree that internal controls should be periodically reviewed to ensure they are operating effectively and enhanced as needed. The Contractor Business System Determination Timeline Tracking tool is an internal control we developed to help ensure contracting officers take appropriate and timely actions regarding business system determinations. This tool first became effective via a tasking memorandum in August 2013 and subsequent tasking memorandums in May 2014 and March 2015 clarified requirements. Contracting officers responsible for business system determinations are required to populate the tool from receipt of a Defense Contract Audit Agency (DCAA) audit report to issuance of a final determination with notes and supporting information. They are required to include in the tool any existing open business system reports for which a final determination has not yet been made. Worth noting, however, the sample of reports selected for evaluation predate implementation of this internal control, and those that were not included on the tool but should have been can mostly be attributed to the learning curve required for using the tool.

Since inception of this tracking requirement, we have been working diligently to ensure all open business system reports are captured on the tool. DCMA Directorates (e.g., DCMA Operations Directorate) are responsible for monitoring data input and ensuring contracting officers add accurate and complete data into the tool. Directorate representatives consolidate this data and compare to what is in the Contract Audit Follow Up (CAFU) eTool, which is a tool that receives new audit report records from DCAA and assigns them to contracting officers. Any data discrepancies between the CAFU eTool and the Contractor Business System Determination Timeline Tracking tool are researched and resolved to ensure open business system reports are properly captured. Additionally, senior leadership conducts regular meetings to review the information in the tracking tool and develops corrective actions as needed. In fact, from October 2014 to June 2015, we issued 843 final determinations of which 740 were within the 70 day timeline goal set forth in policy. This performance reflects an 88% timeliness rating.

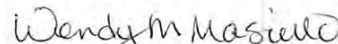
Lastly, we have made great strides in developing and enhancing policy for Board of Review (BoR) requirements. DCMA Instruction 134, BoR provides policy that contracting officers must follow for obtaining appropriate management review on certain contracting actions. For business system reviews, this Instruction provides guidance when contracting officers reject the advice of an auditor. An example of rejection of advice is when a contracting officer and auditor disagree as to whether a deficiency in a business system exists, which would warrant a BoR. A BoR is not warranted if both parties agree that a deficiency exists but one party believes it is a significant deficiency and the other believes it is not a significant deficiency. This Instruction further provides a process flowchart and key control table that identifies areas of risk and possible controls for mitigation.

**DCMA Response: 2.b. Concur.** We did consider requiring BoRs, but after due consideration we determined that to do so was not appropriate as the decision is within the authority and responsibility of the contracting officer. However, a contracting officer can request a BoR if he/she feels the additional advice/support is desired. Furthermore, contracting officer's decisions are subject to review by their CMOs/Centers Leadership and the Agency's Independent Review Team.

## Defense Contract Management Agency (cont'd)

**DCMA Response: 3. Concur.** I agree that appropriate remedial actions should be implemented when contracting officers fail to comply with the Defense Federal Acquisition Regulation Supplement and agency policy for issuing initial and final determinations, obtaining and evaluating the contractor's response, and withholding payments. Remedial action could range from additional reviews, to focused training, to withdrawal of warrant in extreme cases. The remedial actions will be based upon, among other things, the circumstances and the complexity of the situation and whether the noncompliance was willful or not.

For further information regarding DCMA policy on Contractor Business Systems, refer to the DCMA policy publication website at <http://www.dema.mil/policy/>. Please direct any comments or questions to Mary Sheridan, Director, Contracts Policy, at (804) 734-2548 or [Mary.Sheridan@dema.mil](mailto:Mary.Sheridan@dema.mil).

  
Wendy M. Masiello, Lt Gen, USAF  
Director

Attachments: None

## Acronyms and Abbreviations

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- DCAA** Defense Contract Audit Agency
- DCMA** Defense Contract Management Agency
- DFARS** Defense Federal Acquisition Regulation Supplement
- PGI** Procedures, Guidance, and Information

# **Whistleblower Protection**

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